Prince Resource Corporation

Financial Statements

March 31, 1998 and 1997

Collins
Barrow
Chartered Accountants

1400 First Alberta Place
777-8th Avenue S.W.
Calgary, Canada T2P 3R5
Telephone: (403) 298-1500
Fax: (403) 298-5814

AUDITORS' REPORT

To the Shareholders
Prince Resource Corporation

We have audited the balance sheets of Prince Resource Corporation as at March 31, 1998 and 1997 and the statements of loss and deficit and cash flow for the years then ended. These financial statements are the responsibility of the company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with generally accepted auditing standards. Those standards require that we plan and perform an audit to obtain reasonable assurance whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation.

In our opinion, these financial statements present fairly, in all material respects, the financial position of the company as at March 31, 1998 and 1997 and the results of its operations and cash flow for the years then ended in accordance with generally accepted accounting principles.

Collins Barrow

CHARTERED ACCOUNTANTS

Calgary, Alberta
September 28, 1998

Prince Resource Corporation

(Incorporated under the laws of Alberta)

Balance Sheets

March 31, 1998 and 1997

	1998	1997
Assets		
Current assets		
Accounts receivable and prepaid expenses	$ 91,488	$ 112,597
Well abandonment deposit (note 3)	24,270	24,500
Capital assets (note 4)	1,626,359	2,384,013
	$ 1,742,117	$ 2,521,110
Liabilities		
Current liabilities		
Bank indebtedness (note 5)	$ 190,726	$ 107,264
Accounts payable and accrued liabilities	365,378	302,483
	556,104	409,747
Future removal and site restoration	12,020	6,135
Shareholders' Equity		
Share capital (note 6)	3,633,390	3,633,390
Deficit	(2,459,397)	(1,528,162)
	1,173,993	2,105,228
	$ 1,742,117	$ 2,521,110

Approved by the Board,

____________________ Director

____________________ Director

Prince Resource Corporation
Statements of Loss and Deficit
Years Ended March 31, 1998 and 1997

	1998	1997
Revenue		
Oil and gas revenue, net of royalties	$ 314,847	$ 344,689
Alberta royalty tax credit	7,308	16,177
Interest	118	943
Gas processing income (loss), net	(21,265)	19,047
	301,008	380,856
Expenses		
Operating	325,484	339,683
General and administrative	178,213	143,620
Depletion and depreciation	587,995	92,015
	1,091,692	575,318
Loss before the following	(790,684)	(194,462)
Loss on disposal of capital assets	(140,551)	-
Net loss	(931,235)	(194,462)
Deficit, beginning of year	(1,528,162)	(1,333,700)
Deficit, end of year	$ (2,459,397)	$ (1,528,162)
Net loss per share (note 6[f])	$ (0.05)	$ (0.01)

Prince Resource Corporation
Statements of Cash Flow
Years Ended March 31, 1998 and 1997

	1998	1997
Operating activities		
Net loss	$ (931,235)	$ (194,462)
Add items not affecting cash		
Depletion and depreciation	587,995	92,015
Loss on disposal of capital assets	140,551	-
Cash flow used in operations	(202,689)	(102,447)
Net change in non-cash working capital balances related to operating activities	108,806	2,526
	(93,883)	(99,921)
Financing activities		
Issuance of share capital	-	1,540,000
Share issuance costs	-	(4,700)
	-	1,535,300
Investing activities		
Well abandonment deposit	230	(24,500)
Acquisition of capital assets	(32,824)	(1,817,477)
Proceeds from disposition of capital assets	67,817	-
Net change in non-cash working capital balances related to investing activities	(24,802)	196,953
	10,421	(1,645,024)
Cash outflow	(83,462)	(209,645)
Cash (bank indebtedness), beginning of year	(107,264)	102,381
Bank indebtedness, end of year	$ (190,726)	$ (107,264)

1. Future operations

These financial statements have been prepared on the basis of accounting principles applicable to a "going concern", which assume that the company will be able to realize its assets and discharge its liabilities in the normal course of operations.

The company has incurred significant operating losses in the years ended March 31, 1998 and 1997, and as at March 31, 1998, has a working capital deficiency of $464,616. The continued existence of the company is dependent upon its ability to achieve one or several of the following:

(a) Management's ability to optimize current oil and gas exploration, development and operating activities.

(b) Management's ability to successfully negotiate favourable selling prices for existing oil and gas interests to secure funds to discharge current obligations.

(c) Management's ability to successfully complete the development of the International Trade Center in Shanghai, China (note 8[b]).

Failure of management to reorganize or restructure current operations as described above may result in financial difficulties which would make the use of the "going concern" assumption invalid. If the "going concern" assumption was not appropriate for these financial statements, then adjustments would be necessary to the carrying value of assets and liabilities, reported revenues and expenses and the balance sheet classifications used.

2. Significant accounting policies

(a) Exploration and development costs

The company follows the full cost method of accounting for exploration and development expenditures, whereby all costs related to the exploration for and the development of oil and gas reserves in Canada are initially capitalized. Costs capitalized include land acquisition costs, geological and geophysical expenditures, rentals on undeveloped properties, costs of drilling productive and non-productive wells, together with overhead and interest directly related to exploration and development activities and lease and well equipment.

Costs capitalized are depleted and depreciated using the unit-of-production method based on estimated proven gross oil and gas reserves as determined by independent and company engineers. For purposes of the calculation, oil and gas reserves are converted to a common unit of measure on the basis of their relative energy content. Gains or losses are not recognized upon disposition of oil and natural gas properties unless such a disposition would significantly alter the rate of depletion and depreciation.

Costs subject to depletion under the full cost method also include estimated future removal and site restoration costs, net of expected recoveries. This would include the costs of production equipment removal and environmental cleanup based upon existing regulations and economic circumstances at year end. The current year's provision for future site restoration costs is included in depletion and depreciation expense.

In applying the full cost method, the company performs a ceiling test which restricts the capitalized costs less accumulated depletion and depreciation for each cost centre from exceeding an amount equal to the estimated undiscounted value of future net revenues from proven oil and gas reserves, based on current prices and costs, after deducting estimated future general and administrative expenses, future removal and site restoration costs, financing costs and income taxes ("cost ceiling").

The amounts recorded for depletion and depreciation of exploration and development costs, the provision for future removal and site restoration costs and the ceiling test are based on estimated proven reserves, production rates, future oil and gas prices and future costs. By their nature these estimates are subject to measurement uncertainty and changes in those estimates may have a material impact on the financial statements of future periods.

(b) Depreciation

The gas plant is depreciated using the straight-line method over its estimated useful life of 15 years. Other equipment is depreciated using the declining balance method at rates varying from 20% to 30% per annum.

(c) Joint venture accounting

Substantially all of the company's exploration and production activities are conducted jointly with others and accordingly these financial statements reflect only the company's proportionate interest in such activities.

(d) Income taxes

Income taxes are accounted for using the deferral method of income tax allocation. Under this method, the income tax provision is based on accounting income at current income tax rates without subsequent adjustments to reflect changes in income tax rates.

(e) Flow-through shares

Share capital includes flow-through shares issued pursuant to certain provisions of the Income Tax Act (Canada). The Act provides that, where the share issuance proceeds are used for exploration and development expenditures, the related income tax deductions may be renounced to subscribers. Accordingly, these expenditures provide no income tax deduction to the company.

The value assigned to the properties upon which subscribers' funds were expended is the actual dollar amount of the expenditures with share capital being recorded based on cash received.

3. Well abandonment deposit

The company is required pursuant to Alberta Energy and Utilities Board ("AEUB") regulations, to place on deposit funds which will be applied against future removal and site restoration costs for existing wells. These funds are held in trust by the AEUB and will be released to the company upon satisfaction of certain specified conditions.

4. Capital assets

	1998		
	Cost	Accumulated Depletion and Depreciation	Net Book Value
Petroleum and natural gas properties including exploration and development thereon	$ 2,897,800	$ 1,643,263	$ 1,254,537
Lease and well equipment	508,467	263,004	245,463
Gas plant	160,178	39,210	120,968
Other equipment	15,691	10,300	5,391
	$ 3,582,136	$ 1,955,777	$ 1,626,359

	1997		
	Cost	Accumulated Depletion and Depreciation	Net Book Value
Petroleum and natural gas properties including exploration and development thereon	$ 2,876,803	$ 1,169,461	$ 1,707,342
Lease and well equipment	527,752	166,741	361,011
Gas plant	379,101	71,279	307,822
Other equipment	16,791	8,953	7,838
	$ 3,800,447	$ 1,416,434	$ 2,384,013

Capital assets having a net book value of $641,678 (1997 - $1,187,450) for accounting purposes have a $NIL cost for income tax purposes.

Future removal and site restoration costs are estimated in aggregate to be $242,120 (1997 - $222,500) of which $5,885 (1997 - $4,700) was charged to income for the year.

5. Bank indebtedness

	1998	1997
Bank overdraft (cash)	$ 28,226	$ (12,736)
Demand revolving bank loan	162,500	-
Demand non-revolving bank loan	-	120,000
	$ 190,726	$ 107,264

The demand revolving bank loan is available to a maximum amount of $300,000. The loan is repayable in monthly principal reductions of $12,000 and bears interest at a Canadian chartered bank's prime rate plus 1.5% per annum. The loan is secured by a general security agreement covering all present and future property of the company, a first fixed and floating charge debenture in the amount of $500,000 over all of the company's assets and an assignment of insurance.

Under the demand revolving bank loan agreement, the company is in violation of the net revenue coverage covenant and certain compliance related loan covenants.

6. Share capital

(a) Authorized
Unlimited common voting shares
Unlimited preferred shares

(b) Issued

	Number	Stated Value
Common shares		
Balance, March 31, 1996	10,169,193	$ 2,215,257
Issued for petroleum and natural gas properties and equipment [note 6(c)]	7,500,000	1,500,000
Issued to consultant for services rendered [note 6(c)]	200,000	40,000
Balance, March 31, 1997 and 1998	17,869,193	3,755,257
Less: Share issuance costs		
Balance, March 31, 1997 and 1998		143,643
Tax benefit from deducting share issuance costs		(21,776)
		121,867
Balance, March 31, 1997 and 1998		$ 3,633,390

(c) Pursuant to a purchase and sale agreement dated April 30, 1996, the company acquired certain petroleum and natural gas properties and equipment for total consideration of $1,670,000. As partial consideration for this acquisition, the company issued 7,500,000 common shares at an attributed value of $0.20 per share. The common shares were issued pursuant to Section 85(1) of the Income Tax Act (Canada) and have a stated value of $700,000 for income tax purposes. The company also issued 200,000 common shares at an attributed value of $0.20 per share to a consultant as a commission on this acquisition.

(d) As at March 31, 1998, the following options to purchase common shares have been granted to directors, officers and consultants:

Number	Exercise Price Per Share	Expiry Date
205,000	$0.35	April 25, 1999
1,090,000	$0.10	March 25, 2003

(e) As at March 31, 1998, NIL (1997 - 579,004) common shares remain in escrow.

(f) Net loss per share is calculated using the weighted average number of common shares of 17,869,193 (1997 - 17,236,316) outstanding during the year. The exercise of stock options would not be dilutive.

7. Income taxes

Income tax expense differs from that which would be expected from applying the effective Canadian federal and provincial income tax rates of 44.62% to the company's loss before income taxes. The difference results from the following:

	1998	1997
Expected income tax recovery	$ (415,517)	$ (86,769)
Decrease resulting from:		
Non-deductible crown payments net of Alberta royalty tax credit	5,090	3,601
Resource allowance	20.220	-
Depletion and depreciation on non-tax based assets	133.608	12.705
Loss on disposal of capital assets	30,491	-
Deferred tax benefit not recognized	225,751	69,972
Other	357	491
	$ -	$ -

The income tax benefit from share issuance costs is deducted from share issuance costs when realized. Share issuance costs available for deduction against future taxable income, for which no benefit has been recognized in the financial statements total $94,532.

The financial statements do not reflect potential tax reductions available through the application of losses carried forward against future years' earnings otherwise subject to income taxes. The losses expire as follows:

2003	$ 39,806
2004	87,588
2005	173,894
	$ 301,288

8. Commitments

(a) On August 20, 1998, the company entered into a new lease for office space and is obligated to make minimum annual rental payments exclusive of occupancy costs as follows:

1999	$ 6,476
2000	11,565
2001	12,357
2002	13,613
2003	5,948
	$ 49,959

(b) Pursuant to a letter agreement dated February 8, 1998, the company commited to the development of an international second-hand equipment trade center in Shanghai, China. The terms of this letter are as follows:

(i) The company will issue an aggregate of 22,500,000 common shares at $0.20 per share for total consideration of $4,500,000;

(ii) The company will issue $20,000,000 U.S. of 10% convertible, redeemable, retractable debentures with a five year term. The debentures will be convertible into common shares one year from the start of commercial operations based on a formula using net earnings per share. The company will have the option to redeem the debentures if they are not converted within the term specified;

(iii) $850,000 of the initial funds raised in (i) will be held in trust, releasable to the company upon completion of the funding requirements for this project and upon receipt of regulatory approval;

(iv) At the completion of these transactions, the company will issue 2,400,000 options to officers and directors of the company to purchase common shares at $0.35 per share expiring five years from the date of issue; and

(v) Upon completion of the financing arrangements, the company will proceed with the development of the Shanghai Trade Center.

These transactions are subject to regulatory and shareholder approval in addition to satisfactory results from a project feasibility study.

9. Related party transactions

(a) During the year, the company paid $7,121 (1997 - $2,590) in legal and consulting fees to directors of the company and $30,000 (1997 - $NIL) in administrative fees to a company related by virtue of having a common officer and director of each entity. Management is of the opinion that these transactions were undertaken under the same terms and conditions as transactions with non-related parties.

(b) Included in accounts payable and accrued liabilities as at March 31, 1998 is $23,617 (1997 - $21,826) due to a company related by virtue of having a common officer and director of each entity. This amount is unsecured, non-interest bearing and due upon demand.

10. Financial instruments

(a) Fair values

The fair values of accounts receivable, bank indebtedness and accounts payable and accrued liabilities are estimated to approximate their carrying values due to the short-term nature of these financial instruments.

(b) Credit risk

The company's exposure to credit risk is limited to the carrying value of accounts receivable in the amount of $91,488 (1997 - $112,597).

(c) Interest rate risk

The company is exposed to interest rate cash flow risk to the extent that the demand revolving bank loan is at a floating rate of interest.

11. Uncertainty due to the Year 2000 Issue

The Year 2000 Issue arises because many computerized systems use two digits rather than four to identify a year. In addition, similar problems may arise in some systems which identify certain dates in 1999 to represent something other than a date. The effects of the Year 2000 Issue may be experienced prior to, on or subsequent to January 1, 2000. It is not possible to be certain that all aspects of the Year 2000 Issue affecting the entity, including those related to the efforts of customers, suppliers or other third parties, will be fully resolved. Therefore, the company's ability to conduct normal business operations may be impacted. This impact may range from significant system failure to minor errors.

12. Comparative figures

The presentation of certain accounts of the previous year has changed to comform with the presentation adoped for the current year.